No. 14,972

IN THE

United States Court of Appeals

For the Ninth Circuit

JAMES F. CRAFTS,
Appellant,

vs.

FEDERAL TRADE COMMISSION,
Appellee.

On Appeal from an Order Enforcing Subpoena.

BRIEF FOR INSURANCE COMMISSIONER OF THE STATE OF CALIFORNIA AND THE ATTORNEY GENERAL OF THE STATE OF CALIFORNIA, AS AMICI CURIAE.

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INTRODUCTORY.

Pursuant to information furnished by the Clerk of this Court, that this Court follows the United States Supreme Court rule allowing the Attorney General of a state to file an amicus curiae brief in any cause in respect to which the law of his state is involved and where the state correspondingly has an interest, without previously procuring permission of the Court, this brief is filed in the above cause. In the event

formal permission is required, it is prayed that such permission be granted and this brief filed accordingly.

However, this is not the first appearance of the Attorney General as counsel for the Insurance Commissioner in this cause. Permission to file such a brief in the event the matter came to the briefing stage was sought and granted in the proceeding before the Federal Trade Commission (Record, 27).

It is for these amici curiae briefly to explain the vital State interest developed in this cause as they view it. That explanation will also explain why this filing has been delayed until after the filing of the brief for appellee in the cause.

The reason and explanation of the primary interest of the State of California, and correspondingly of its officers represented by this brief, is in the vindication of the power of the State of California to control its domestic insurance companies by and through its police power regulations, statutory or administrative.

The Insurance Commissioner of the State of California requested that the Attorney General appear in this cause for the purpose of assisting the Court by expressing the State's views on the question involved. The Attorney General, being the principal law enforcement agent for the State of California, has determined not to engage in a jurisdictional dispute with a federal law enforcement agency in connection with regulation of a California insurance company. Consequently, although this brief will refer to, and possibly discuss somewhat, the problems involved in the issue of exclusive State jurisdiction which has been

tendered by appellant, the primary purpose of the brief is to develop, for the assistance of the Court, the law governing the State of California in respect to its own power over its own corporate creatures, its California insurers. If, under the terms of the McCarran Act, the extent of this power is such that the Federal Trade Commission Act is not applicable to these insurers, that is a matter for the parties to argue and this Court to determine. The vital interest of the State is in the vindication of its own power rather than to squabble over the jurisdiction of a federal agency which, under the terms of the McCarran Act, appears to be granted a somewhat limited jurisdiction. Consequently this brief could not be filed until the appellee in its brief indicated whether or not its contentions as to the power granted the Federal Trade Commission—not the scope of the Congressional power, as to which there appears to be no issue in this case—was bottomed on any claim of a lack of applicable regulation by the State of California in respect to the subject matter here involved.

Unfortunately, while appellee does not appear to clearly state its contentions in this respect, it does appear to bottom its claim of jurisdiction upon the theory that sections 780, et seq. of the California Insurance Code cannot have extraterritorial effect:

> "We do not argue that the California statute is unconstitutional, but appellant's interpretation of the California statute attempts to give it an extraterritorial effect which even the cases cited by appellant . . . do not sustain" (Br. for Appellee, pp. 16-17).

Nor is appellee's contention made clearer by quotations from *St. Louis Cotton Compress Co. v. Arkansas,* 260 U.S. 346, relating to lack of state power over *foreign* corporations, and from *United States v. South-Eastern Underwriters Association,* 322 U.S. 533, relating to *congressional* power (Br. for Appellee, p. 17), inasmuch as it is *California's* regulation of a *domestic* insurer that is here involved. It is not *congressional* power but the extent of the jurisdiction *which Congress has delegated* to the Federal Trade Commission which is, presumably, the issue.

The *power* of the United States, as we understand it, is not questioned. The *South-Eastern Underwriters Association* case seems to have settled that.

But that case, and the cases succeeding, make it quite clear that neither the Supreme Court, in that case, nor Congress under the McCarran Act, intended that the relationships of the federal and state regulatory agencies to insurance business would be the same as such relationships in the case of a number of other businesses (*United States v. South-Eastern Underwriters Association,* 323 U.S. 533, 562; *Prudential Ins. Co. v. Benjamin,* 328 U.S. 408, 431-436; *Robertson v. California,* 328 U.S. 440, 462). This brief, therefore, is written solely for the purpose of upholding in this Court the State's contention that misrepresentation in advertising by an insurer domestic to California is regulated by sections 780 and following of the California Insurance Code; that this regulation follows and applies to such domestic insurer in every state or territory in which it does business; and that this extra-

territorial effect of that regulation is in accord with the Constitution of the United States and its laws as interpreted by the United States Supreme Court.[1]

[1]The advisability of presenting in this case the law supporting this principle was forcibly impressed upon amici curiae here by the sweeping expressions of the majority of the appellee commission in their Docket No. 6237, *In the Matter of the American Hospital and Life Insurance Co.,* this last April 24th: "Certainty the States lack the power to tax or regulate purely interstate activities of insurance companies. It can only be that the section (McCarran Act) provides that State authority over *intrastate* insurance business that might affect interstate insurance business could not be disturbed by Federal legislation which did not specifically mention insurance" (Typed Opinion p. 4. That Matter, like the instant cause, concerned only advertising by an insurance company).

Since the Commission is not a judicial body (*Federal Trade Com'n v. Eastman Kodak Co.,* 274 U.S. 619), such assumptions of legal principles by such an administrative agency should lack even persuasive power in this or any other court. Yet such peculiar administrative pronouncements do illustrate the necessity for state participation in cases of this nature to assist the Court, so far as lies in counsel's power, to avoid disturbance of such long-standing "pre-McCarran Act" legal principles as the right of the state to tax interstate remittances related to transactions partly within the State (*Equitable Life Society v. Pennsylvania,* 238 U.S. 143; *Compania General de Tobacos v. Collector,* 275 U.S. 87, 98), or based upon jurisdiction over a domestic corporation (*Guardian Life Ins. Co. v. Chapman,* 302 N.Y. 226, 97 N.E.2d 877; *Western Travelers Acc. Assn. v. Johnson,* 14 Cal.App.2d 306, 58 Pac.2d 206, Cal. Supreme Ct. hear. den.) and the power to enforce state-promulgated standards having extraterritorial impact upon insurance companies where a proper local interest appears (*Hoopeston Canning Co. v. Cullen,* 318 U.S. 313; *State Farm Mut. Auto. Ins. Co. v. Deuel,* 324 U.S. 154).

I.

SECTIONS 780 AND 781 OF THE CALIFORNIA INSURANCE CODE PROMULGATE RULES OF CONDUCT WHICH COVER ADVERTISING BY CALIFORNIA INSURERS AND WHICH ARE NOT INTENDED TO BE LIMITED IN THEIR EFFECT TO CONDUCT WITHIN THE STATE OF CALIFORNIA.

There would seem to be no question that misrepresentation in advertising is included in the misrepresentations forbidden by sections 780 and 781 of the California Insurance Code.[2] In *United Insurance Co. v. Maloney,* 127 Cal.App.2d 155, 273 Pac.2d 579, the court points out that the accusations "resolve themselves into a claim that in its advertisements, circulars and in the representations by the agents the policies are represented as covering all sickness and health and no mention is made of the exceptions . . ." (127 Cal.App.2d 155, 156, 273 Pac.2d 579).

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[2]Sec. 780

An insurer or officer or agent thereof, or an insurance broker or solicitor, shall not cause or permit to be issued, circulated or used, any misrepresentation of the following:

(a) The terms of a policy issued by the insurer or sought to be negotiated by the person making or permitting the misrepresentation.

(b) The benefits or privileges promised thereunder.

(c) The future dividends, payable thereunder.

Sec. 781

A person shall not make any misrepresentation (a) to any other person for the purpose of inducing, or tending to induce, such other person either to take out a policy of insurance, or to refuse to accept a policy issued upon an application therefor and instead take out any policy in another insurer, or

(b) To a policyholder in any insurer for the purpose of inducing or tending to induce him to lapse, forfeit or surrender his insurance therein.

A person shall not make any representation or comparison of insurers or policies to an insured which is misleading, for the purpose of inducing or tending to induce him to lapse, forfeit, change or surrender his insurance, whether on a temporary or permanent plan.

Likewise, during the years 1952 and 1953 accusations were issued, and proceedings taken, by the California Insurance Commissioner, against a number of both domestic and foreign insurance companies, arising out of complaints or misrepresentations in advertising.[3]

Particularly to be noted is the rather careful draftsmanship of the California Insurance Code regulatory provisions (1) in respect to their application to domestic and foreign insurers, and (2) in respect to such application of the provisions thereof to California only, or to California together with other states in which the insurer may be operating.

Examples of this draftsmanship and the consequent clarity of meaning as to application are found particularly in sections 703, 704, 801, 827, 880, 1010, and 1153 of the Code.

Section 704,[4] for instance, deals with the general conduct of the business. It obviously refers to any

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[3]In the Matter of the Certificate of Authority of . . . Hearthstone Insurance Company of Massachusetts, No. S.F.6683 ABP; In the Matter of the Certificate of Authority of . . . Westland Insurance Co., No. SF-4228 ABC-P; In the Matter of the Certificate of Authority of . . . World Insurance Company of Omaha, Nebraska, No. S.F.4259-ABC.P; In the Matter of the Certificate of . . . National Travelers Insurance Company, No. LA-5947; In the Matter of the Certificate of Authority of . . . Constitution Life Insurance Co., No. SF 3333-CP. All the foregoing were administrative proceedings before the California Department of Insurance. Some are still in litigation in the California courts, but in none of these matters was there any contention made that section 780 of the Insurance Code does not appertain to advertising.

[4]Sec. 704

The commissioner may suspend the certificate of authority of an insurer for not exceeding one year whenever he finds, after proper

insurance company, whether foreign or domestic, and applies to any business that company does, whether in or out of the state.

Section 703[5], on the other hand, by its terms is limited to certain business "when done in this state".

Section 801[6] expressly applies to "admitted" insurers, the term "admitted" being defined by section 24 of the Code to apply to the status of being able to transact insurance business in the State of Cali-

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hearing following notice, that such insurer engages in any of the following practices:

(a) Conducting its business fraudulently.

(b) Not carrying out its contracts in good faith.

(c) Habitually and as a matter of ordinary practice and custom compelling claimants under policies to either accept less than the amount due under the terms of the policies or resort to litigation against such insurer to secure the payment of the amount due.

The order of suspension shall prescribe the period of such suspension.

The proceedings shall be conducted in accordance with Chapter 5 of Part 1 of Division 3 of Title 2 of the Government Code, and the commissioner shall have all the powers granted therein.

[5]Sec. 703

Except when performed by a surplus line broker, the following acts are misdemeanors when done in this State:

(a) Acting as agent for a non-admitted insurer in the transaction of insurance business in this State.

(b) In any manner advertising a non-admitted insurer in this State.

(c) In any other manner aiding a non-admitted insurer to transact insurance business in this State.

In addition to any penalty provided for commission of misdemeanors, a person violating any provision of this section shall forfeit to this State the sum of five hundred dollars, together with one hundred dollars for each month or fraction thereof during which he continues such violation.

[6]Sec. 801

Except as provided by this article, an admitted insurer shall not cause to be executed or renewed any contract of insurance covering subject matter located in this State at the time of execution or renewal except either (a) through a resident agent, or (b) after approval in writing by such an agent.

fornia. Consequently, it applies to licensed companies whether foreign or domestic and, not being limited to acts within the State, is applicable to contracts involved wherever written so long as an admitted insurer is a party.[7]

Section 880,[8] again, expressly refers to business "in this state".

But section 1010[9] would apply the conservatorship and liquidation law to both foreign and domestic insurers, and the acts specified in section 1011[10] ob-

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[7]Extraterritorial application approved of a similar statute in *Osborn v. Ozlin,* 310 U.S. 53.

[8]Sec. 880.

Except as provided in this article, every insurer shall conduct its business in this State in its own name.

[9]Sec. 1010

The provisions of this article shall apply to all persons subject to examination by the commissioner, or purporting to do insurance business in this State, or in the process of organization with intent to do such business therein, or from whom the commissioner's certificate of authority is required for the transaction of business, or whose certificate of authority is revoked or suspended.

[10]Sec. 1011

The superior court of the county in which is located the principal office of such person in this State shall, upon the filing by the commissioner of the verified application showing any of the following conditions hereinafter enumerated to exist, issue its order vesting title to all of the assets of such person, wheresoever situated, in the commissioner or his successor in office, in his official capacity as such, and direct the commissioner forthwith to take possession of all of its books, records, property, real and personal, and assets, and to conduct, as conservator, the business of said person, or so much thereof as to the commissioner may seem appropriate, and enjoining said person and its officers, directors, agents, servants, and employees from the transaction of its business or disposition of its property until the further order of said court:

(a) That such person has refused to submit its books, papers, accounts, or affairs to the reasonable inspection of the commissioner or his deputy or examiner.

viously may take place in California or elsewhere.[11]

Again, note the careful specification of the application and subject matter illustrated by sections 1150, 1151.6, 1152, and 1153.[12] Others could be cited. Thus

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(b) That such person has neglected or refused to observe an order of the commissioner to make good within the time prescribed by law any deficiency in its capital if it is a stock corporation, or in its reserve if it is a mutual insurer.

(c) That such person, without first obtaining the consent in writing of the commissioner, has transferred, or attempted to transfer, substantially its entire property or business, or, without such consent, has entered into any transaction the effect of which is to merge, consolidate, or reinsure substantially its entire property or business in or with the property or business of any other person.

(d) That such person is found, after an examination, to be in such condition that its further transaction of business will be hazardous to its policy holders, or creditors, or to the public.

(e) That such person has violated its charter or any law of the State.

(f) That a certificate of authority of such person has been revoked under section 10711.

(g) That any officer of such person refuses to be examined under oath, touching its affairs.

(h) That any officer or attorney-in-fact of such person has embezzled, sequestered, or wrongfully diverted any of the assets of such person.

(i) That a domestic insurer does not comply with the requirements for the issuance to it of a certificate of authority, or that its certificate of authority has been revoked; or

(j) That the last report of examination of any person to whom the provisions of this article apply shows such person to be insolvent within the meaning of Article 13, Chapter 1, Part 2, Division 1 of this Code.

[11]So held in *Rhode Island Insurance Co. v. Downey,* 95 Cal. App.2d 220, 212 Pac.2d 965.

[12]Sec. 1150

"Every admitted incorporated insurer may purchase, hold, or convey real estate only for the following purposes and in the following manner:

(a) The building in which it has its principal office and the land upon which that building stands.

(b) Real estate requisite for its accommodation in the convenient transaction of its business.

(c) Real estate acquired by it, or by any person for it, to secure the payment of loans previously contracted or for moneys due.

it is clear that the provisions of sections 780 and 781 beyond question apply to the activities of the California domestic insurers regardless of whether within or without California.

II.

CALIFORNIA HAS THE POWER AND JURISDICTION TO MAKE ITS REGULATIONS OF ITS DOMESTIC INSURERS' CONDUCT APPLICABLE WHEREVER THE INSURER DOES BUSINESS. OTHER JURISDICTIONS WHICH PERMIT THEM TO TRANSACT BUSINESS THEREIN MUST ACCEPT THIS AS A CHARACTERISTIC OF A CALIFORNIA INSURER PERMITTED TO DO BUSINESS IN THAT JURISDICTION.

The Supreme Court has repeatedly sustained the above principle.

Relf v. Rundle, 103 U.S. 222;

Canada Southern v. Gebhard, 109 U.S. 527;

(d) Real estate purchased at sales upon deeds of trust or upon judgments or decrees obtained for such loans or debts.

(e) Real estate conveyed to it in satisfaction of debts previously contracted in the course of its dealings.

(f) Real estate acquired by gift or devise.

(g) Real estate acquired in part payment of the consideration of the sale of real property owned by it, if each such transaction shall not effect an increase in its investment in such real property.

(h) Upon the written approval of the Insurance Commissioner, real estate requisite or desirable for the protection or enhancement of the value of other real or personal property owned by such insurers.

(i) Real estate and improvements thereon under the provisions and subject to the conditions and limitations of Section 1194.8."

Sec. 1151.6

"Every admitted incorporated insurer may, for the protection or enhancement of the value of real property acquired under the provisions of section 1150, use its funds in such manner as it shall deem proper to repair, alter, remodel, rehabilitate, demolish, purchase furnishings or other personal property for use in or otherwise to improve such real estate."

Royal Arcanum v. Green, 237 U.S. 531;
Modern Woodmen v. Mixer, 267 U.S. 544.

The case of *Relf v. Rundle, supra,* perhaps is the outstanding example of the "charter provision" principle embodied in all the above cases. This is, of course, that the laws of the corporate domicile enter into and are part of its charter and that other jurisdictions into which it is permitted to enter and do business accept these laws as applicable to the powers and restrictions upon the corporation.

Sec. 1152

"Domestic incorporated stock insurers, except those governed by sections 3016, 10530, 12373 and 12465 of this code, shall be governed exclusively by the provisions of this section as to payment or distribution of dividends to stockholders. Such insurers may make dividends only from the surplus of admitted assets in excess of the aggregate of the following:

(a) The aggregate par value of the entire issued or subscribed shares;

(b) A surplus equal to fifty (50) per centum of the aggregate par value of the entire issued or subscribed shares;

(c) A premium reserve on policies in force at least equal to the unearned portions of the gross premiums charged for covering the risks computed by such method as is provided in this code, prescribed by the commissioner in absence of such provision, or on a prorata basis in the absence of such provision or prescription;

(d) Proper reserves for expenses, taxes, and outstanding losses computed as set forth in this code;

(e) Proper reserves for all other liabilities. No dividends shall be declared out of such surplus derived from the mere appreciation in the value of assets not yet realized, nor shall any dividends be declared from any part of such surplus derived from an exchange of assets, unless and until such profits have been realized or unless the assets received are currently realizable in cash."

Sec. 1153

"An insurer shall not be admitted within three years from and after the time when it commences business as an insurer, nor

In that case a law of one state making an officer of that state successor to a defunct insurance company was held to authorize that officer to go into another state and exert that ownership by suit in the courts of the second state, without express permission from the courts or by other law of the second state.

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within three years from and after the time when it is first incorporated, unless assets equal to the sum of its liabilities and the minimum capital and surplus required for admission are maintained in cash or one or more of the following:

(a) Securities specified in Sections 1170 to 1175, inclusive;

(b) Bonds specified in Section 1176 if such bonds are legal for investment of savings banks in this State;

(c) Such securities specified in Sections 1178 to 1202, inclusive, as are legal for investment of savings banks in this State;

(d) Premiums in course of collection, or agents' balances representing premiums, on policies effected not more than 90 days prior to the date on which such premiums or balances are valued for the purpose of this section, and earned service fees receivable, not over 90 days due, and evidences of debt representing such assets;

(e) In the case of a life insurer, the amount of current deferred premiums receivable, after deducting therefrom the amount of the loading;

(f) Interests accrued and dividends declared, receivable on any of the assets specified in subdivisions (a) to (e), inclusive, no part of which interest or dividends has been due in excess of one year;

(g) Amount of reinsurance recoverable from admitted insurers."

III.

SECTION 780 PRESCRIBES A CONDITION TO BE MAINTAINED FOR THE CONDUCT OF AN INSURANCE BUSINESS AS A WHOLE. THE APPLICATION OF SUCH A STANDARD OF DOING BUSINESS IN A STATE HAS BEEN SUSTAINED EVEN AS TO INSURERS FOREIGN TO THAT STATE. THERE IS NO QUESTION OF ITS APPLICATION TO INSURERS DOMESTIC TO CALIFORNIA.

Since this case involves an insurer domestic to California, there should be no difficulty in sustaining the principle here concerned, for obviously California's power over her own domestic corporations is no less than her power over foreign corporations doing business in this state.

Section 780, like Section 704, of the California Insurance Code prescribes a standard of honesty and fair dealing between insurance companies and their insureds or applicants for insurance. Certainly these standards are a reasonable requirement for doing business in the State of California, as important to the protection of its citizens as the requirements that reserves on out-of-state insurance business be maintained by a foreign insurer in an out-of-state office, and that such reserves meet specified minimum standards. These last requirements have been held to be within the ambit of state power. *State Farm Mutual Insurance Co. v. Deuel,* 324 U.S. 154.

California, as stated above, can establish certain standards applicable to any insurance company doing business in California in order to protect the citizens of California. These standards naturally apply to a domestic insurer such as Fireman's Fund, but in ap-

plying these standards to a domestic insurer California is interested not only in the protection of the citizens of California but is also interested in the growth and safety of the company. The fact that the application of these standards may affect business or interests in other states has been sustained against constitutional objection.[13]

Hoopeston Canning Co. v. Cullen, 318 U.S. 313, 319-321;

Robertson v. California, 328 U.S. 440.

CONCLUSION.

It is respectfully submitted that whatever jurisdiction the Federal Trade Commission may have, if any, over the appellant under the Federal Trade Commission Act, such jurisdiction cannot rest either upon the lack of applicable state regulation of appellant's

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[13]This, of course, does not mean that there are no restraints upon the state's control of foreign insurers in respect to extraterritorial acts. However, the *St. Louis Cotton Compress Co.* case and *Allgeyer v. Louisiana* case, cited by appellee as limiting extraterritorial application of state regulations to *foreign* insurers (Br. for Appellee, p. 19), have always been put to one side when urged to strike down *extraterritorial* application of state power to protect a legitimate interest of the citizens of the state. Certainly the requirement of honesty in dealing with prospective insureds, everywhere, the requirement of section 780, California Insurance Code, is such an interest. *Osborn v. Ozlin,* 310 U.S. 53; *State Farm Mutual Insurance Co. v. Deuel,* 324 U.S. 154; *Compania General de Tobacos v. Collector,* 275 U.S. 87, 98.

advertising, or upon any lack of California's jurisdiction over the appellant to enact and enforce such regulation.

Dated, San Francisco, California,
May 28, 1956.

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